No. 85-1896

Supreme Court, U.S.
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IN THE

Supreme Court of the United States

OCTOBER TERM, 1985

SECURITIES AND EXCHANGE COMMISSION,
Plaintiff,

v.

WALTER WENCKE, et al.,
Defendants.

THEODORE deLUSIGNAN,
Petitioner,

v.

R. N. GOULD, Receiver-Trustee,
Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

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QUESTIONS PRESENTED

1. Does a district court have jurisdiction and power to order post-judgment "disgorgement" affecting and disposing of property of persons who were not parties to the action?

2. Does a district court violate the Federal Rules of Civil Procedure by effecting "disgorgement" against nonparties through summary proceedings rather than the normal plenary civil action?

3. Does the taking of petitioner's property by summary proceeding violate his Due Process rights of adequate notice and opportunity for hearing under the United States Constitution?

LIST OF PARTIES

The parties to the proceedings below were the petitioner Theodore deLusignan and the respondent R. N. Gould, who is a receiver and trustee appointed by the United States District Court for the Southern District of California.

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PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

Petitioner Theodore deLusignan respectfully prays that a writ of certiorari issue to review the judgment and opinion of the United States Court of Appeals for the Ninth Circuit, entered in the above-entitled proceeding on February 19, 1986.

OPINIONS BELOW

The opinion of the Court of Appeals for the Ninth Circuit is reported at 783 F.2d 829 and is reprinted in the Appendix, p. A-1, *infra*. The Order Adopting Findings of Fact, Conclusions of Law and Recommendations Re Receiver's Application No. 4 in Disgorgement of the United States District Court for the Southern District of California (Thompson, D.J.) has not been reported. It is reprinted in the appendix hereto, p. B-1, *infra*.

JURISDICTION

The district court found federal question subject matter jurisdiction over the underlying action pursuant to Section 22(a) of the Securities Act [15 U.S.C. § 77v(a)] and Section 27 of the Securities Exchange Act [15 U.S.C. § 78aa]. Jurisdiction over the disgorgement proceeding directed against petitioner was claimed under the concept of ancillary jurisdiction. On November 7, 1983, the district court entered its "Order Adopting Findings of Fact, Conclusions of Law and Recommendations Re Receiver's Application No. 4 in Disgorgement."

On petitioner's appeal, the Ninth Circuit on February 19, 1986 entered its judgment and opinion affirming that order of the district court. No petition for rehearing was sought.

Jurisdiction of this Court to review the judgment of the Ninth Circuit is provided by 28 U.S.C. § 1254(1).

CONSTITUTION AND STATUTES INVOLVED

Fifth Amendment, United States Constitution:

No person shall be . . . deprived of life, liberty, or property, without due process of law. . . .

Rule 1, Federal Rules of Civil Procedure:

These rules govern the procedure in the United States District Courts in all suits of a civil nature whether cognizable as cases of law or in equity or in admiralty, with the exceptions stated in Rule 81. They shall be construed to secure the just, speedy, and inexpensive determination of every action.

Rule 2, Federal Rules of Civil Procedure:

There shall be but one form of action to be known as "civil action."

Rule 3, Federal Rules of Civil Procedure:

A civil action is commenced by filing a complaint with the court.

Rule 4(a) and (b), Federal Rules of Civil Procedure:

> (a) SUMMONS: Issuance. Upon the filing of the complaint the clerk shall forthwith issue a summons and deliver the summons to the plaintiff or the plaintiff's attorney, who shall be responsible for prompt service of the summons and a copy of the complaint. Upon request of the plaintiff separate or additional summons shall issue against any defendants.
>
> (b) SAME: Form. The summons shall be signed by the clerk, be under the seal of the court, contain the name of the court and the names of the parties, be directed to the defendant, state the name and address of the plaintiff's attorney, if any, otherwise the plaintiff's address, and the time within which these rules require the defendant to appear and defend, and shall notify him that in case of his failure to do so judgment by default will

be rendered against him for the relief demanded in the complaint. When, under Rule 4(e), service is made pursuant to a statute or rule of court of a state, the summons, or notice, or order in lieu of summons shall correspond as nearly as may be to that required by the statute or rule.

STATEMENT OF THE CASE

Petitioner in 1972 was president of Portsmouth Square, Inc. ("PSI"), a corporation which owned a substantial interest in Justice Investors, a partnership which owned the Holiday Inn located at 750 Kearny Street in San Francisco. At that time, PSI suffered from severe financial problems. In May, 1972, petitioner responded to an advertisement in the Wall Street Journal which offered assistance to financially distressed companies. In this way petitioner came to meet Walter Wencke, author of the advertisement and principal defendant in the underlying securities fraud action initiated by the Securities and Exchange Commission.

Wencke proposed to the board of directors of PSI a financial aid arrangement which called for Ramapo, a corporation created by Wencke and entirely owned by the Hansa Trust (a Wencke family trust) to give PSI consideration in the sum of $348,193 consisting of $10,000 cash and assumption of PSI liabilities of $338,193. Also, Ramapo agreed to assist in negotiating a $1.2 million obligation to Fireman's Fund Insurance Company which was in default. In return, PSI was to issue to Ramapo the balance of its authorized and unissued stock which amounted to 401,351 shares, a 53.5% controlling interest in PSI. These included the same shares which the district court ordered to be disgorged after summary proceedings.

Wencke also offered to employ petitioner as an officer of Ramapo, PSI or one of their subsidiaries and to transfer 25 of Ramapo's 100 shares to petitioner. The board of directors of PSI

ratified the terms of the transfer of shares to Ramapo and approved petitioner's proposed employment contract including transfer to him of the 25 Ramapo shares. One board member commented at the time that "any personal benefits Mr. deLusignan might derive are contingent upon his own efforts and success in solving problems of Portsmouth Square." Petitioner served as president of PSI for five more years, until 1977.

The transaction with Ramapo enabled PSI to divest itself of unprofitable subsidiaries, improve its net worth from a negative $323,121 to a positive $25,072 and prevent foreclosure by Fireman's Fund against its only asset of real value, the interest in Justice Investors. Today, PSI is a prosperous dividend-paying corporation with its shares valued at $6 to $7. The Ninth Circuit opinion noted petitioner's contention that by 1977 the hotel property was worth over $50 million and that prior to the summary disgorgement order from which he appealed, his Ramapo shares were worth about $2.6 million. See appendix p. A-3, *infra*.

The SEC in 1976 filed the underlying securities fraud action against Wencke, his wife, three other persons and twenty-five trusts and corporations controlled by Wencke and his associates. It was alleged that Wencke violated state and federal securities law and breached fiduciary duties by diverting assets from entities he controlled including Time-Lenders, Inc. ("Time"), Sun Fruit, Ltd. ("Sun Fruit"), Santa Fe Financial Corporation ("Santa Fe") and using those assets for his personal gain. Petitioner, Ramapo and the Hansa Trust were not named as parties to this action.

In March, 1977, the district court entered a default judgment in the action which permanently enjoined Wencke and the other defendants from engaging in securities activities and ordered that Wencke disgorge all assets or funds that he had taken in breach of his fiduciary duties. This judgment appointed respondent R.N. Gould as receiver of Time, Sun Fruit and Santa Fe. Among other things, he was authorized to take control of the assets of these companies, to operate them, to prosecute any claims they had and

to manage and conserve their assets for the benefit of defrauded investors. Some defendants appealed, and the Ninth Circuit affirmed except as to certain relief which exceeded that requested in the complaint. *Securities & Exch. Comm. v. Wencke*, 577 F.2d 619 (9th Cir. 1978). Petitioner, Ramapo and the Hansa Trust were not parties to this judgment.

In November, 1977, the district court appointed respondent as the voting trustee of 60 shares of Ramapo owned by Wencke or the Hansa Trust, and by 1979 the receiver had acquired an additional 15 Ramapo shares from Paul Potter. This left the respondent in control of 75 shares of Ramapo, and petitioner held the remaining 25 shares.

In March, 1979, the district court ordered that respondent as receiver was authorized to identify assets that Wencke and those acting in concert with him had looted from Time, Sun Fruit and Santa Fe and their subsidiaries and also "ill-gotten gains" derived from such assets and to initiate "disgorgement proceedings" to recover such assets and ill-gotten gains. A magistrate/special master was appointed and authorized to issue any reports regarding disgorgement proceedings to the district court pursuant to Rule 53, Federal Rules of Civil Procedure if the magistrate/special master found them appropriate "for the proper effectuation of the Final Judgment."

On November 4, 1980, respondent filed two documents in the district court. One was Application Number 4 in Disgorgement which was filed as a post-judgment document in the SEC action against Wencke. This was directed against petitioner, Wencke, Ramapo, the Hansa Trust plus other individuals and entities. It asked that the court order disgorgement of Ramapo's corporate charter, the 60 Ramapo shares owned by the Hansa Trust and the 25 shares owned by petitioner.

The other was a complaint which initiated an independent, normal civil action against petitioner, Ramapo and the Hansa Trust

(and others) which prayed for disgorgement of Ramapo's corporate charter and certificates and a declaration imposing a constructive trust over the defendants' Ramapo shares. As the Ninth Circuit noted, this complaint was "virtually identical" to the Application Number Four in Disgorgement.

This Application Number Four in Disgorgement was served on Ramapo and the Hansa Trust in January, 1981 and on petitioner in April, 1981. When served with the Application, petitioner was not served with a summons. In November, 1983, petitioner was served with a summons and the complaint in the independent civil action filed by respondent in 1980.

After service of the Disgorgement Application upon petitioner, two years and four months passed without any action. On August 19, 1983, petitioner was served by mail with another copy of the Disgorgement Application, some supporting documents and a notice of a hearing on the disgorgement application to be held before the magistrate/special master 19 days later.

On September 2, 1983, petitioner filed a Notice of Special Appearance and Objection to Hearing in which he claimed that the district court lacked personal jurisdiction over him and that he was deprived of due process of law. This objection was overruled, and the magistrate/special master proceeded with an evidentiary hearing at which counsel for petitioner did not present evidence or cross-examine witnesses.

Following the hearing, the magistrate/special master adopted findings of fact and conclusions of law which included his recommendation that Ramapo be deemed a constructive trustee for the benefit of defrauded shareholders of Time and Santa Fe and that it be required to disgorge its PSI shares. Although the Application itself had asked for disgorgement of petitioner's 25 shares of Ramapo, the findings and conclusions made no mention of them. As the Ninth Circuit noted, however, the disgorgement of

Ramapo's PSI shares made petitioner's Ramapo shares "virtually worthless." See p. A- , *infra*.

Respondent then moved the district court for adoption of the findings, conclusions and recommendations, and a hearing was held on the motion 17 days later. Petitioner filed a notice of special appearance and objected on the grounds that the court lacked personal jurisdiction over him and that the manner in which the disgorgement proceedings were conducted violated his due process rights and the Federal Rules of Civil Procedure. On November 7, 1983, the district court rejected petitioner's claims, adopted the findings, conclusions and recommendations and ordered that Ramapo disgorge its PSI shares and any profits.

This order was appealed to the Ninth Circuit and affirmed. Other than cases cited in footnotes, the only authority cited by the Ninth Circuit to justify its rejection of petitioner's claims was another decision of that Circuit, *S.E.C. v. Universal Financial*, 760 F.2d 1034 (9th Cir. 1985).

REASONS FOR GRANTING THE WRIT

I.

BY APPROVING RELIEF AGAINST A NONPARTY, THE NINTH CIRCUIT HAS EXCEEDED ITS JURISDICTION IN A MANNER WHICH CONFLICTS WITH DECISIONS OF THIS COURT AND OTHER CIRCUITS

Because petitioner and Ramapo were not parties to either the underlying action or the default judgment, the district court had no power to order disgorgement of Ramapo's PSI shares which had the effect of rendering petitioner's shares in Ramapo worthless. The doctrine of ancillary jurisdiction cannot invest the court with power over petitioner because there was no other proceeding

against him to which the disgorgement proceeding could be ancillary. The Ninth Circuit rejected respondent's claims to *in rem* jurisdiction (see appendix p. A-7, n. 5, *infra*), so the power to adjudicate this controversy must proceed from *in personam* jurisdiction.

Action taken by a court against a person not a party to the action is barred by fundamental concepts of due process under the United States Constitution. In *Hansberry v. Lee*, 311 U.S. 32 (1940) this Court held that petitioners who sought to invalidate racially restrictive real property covenants were not bound under *res judicata* principles by a judgment in a prior action in which they were neither parties nor adequately represented by those who were parties. The Court stated:

> "It is a principle of general application in Anglo-American jurisprudence that one is not bound by a judgment *in personam* in a litigation in which he is not designated as a party or to which he has not been made a party by service of process. *Pennoyer v. Neff*, 95 U.S. 714; 1 Freeman on Judgments (5th ed.), §407. A judgment rendered in such circumstances is not entitled to the full faith and credit which the Constitution and Statute of the United States, R.S. §905, 28 U.S.C. §687, prescribe [citations]; and judicial action enforcing it against the person or property of the absent party is not that due process which the Fifth and Fourteenth Amendments require. *Postal Telegraph Cable Co. v. Newport*, 247 U.S. 464; *Old Wayne Mutual Life Assn. v. McDonough*, 204 U.S. 8."
>
> *Hansberry v. Lee, supra*, 311 U.S. at 40-41.

These principles were applied in *Zenith Radio Corp. v. Hazeltine*, 395 U.S. 100 (1968). There Hazeltine Research, Inc. ("HRI") was a named cross-defendant in an action. Hazeltine

Corporation, parent of HRI, was not a party, was not served and did not participate in the trial. The district court, however, adopted findings of fact and conclusions of law naming Hazeltine Corporation as a person against whom the judgment would be entered on an alter ego theory, *Hazeltine Research, Inc. v. Zenith Radio Corporation*, 388 F.2d 25, 28-30 (7th Cir. 1967).

Hazeltine Corporation moved to vacate the judgment against it and filed provisional appeals from the judgments. The court of appeals held that since Hazeltine Corporation was neither named nor served, the sole basis for liability on the judgment was the theory that HRI was its alter ego. The court held that Hazeltine Corporation was not adequately represented on this issue, that resolution of the alter ego issue could be made only after an adversary determination of the facts involved, and the district court did not make such a determination. *Id.* at 30. The court also stated that because Hazeltine Corporation did not control the litigation it could not be joined in the judgment, and there was no reason why the corporation's disclosure of files in obedience to subpoenas would bind the corporation when it was not joined as a party. *Id.*

It was held that the court of appeals was correct in vacating the judgments:

> "It is elementary that one is not bound by a judgment *in personam* resulting from litigation in which he is not a party or to which he has not been made a party by service of process. *Hansberry v. Lee*, 311 U.S. 32, 40-41 (1940). The consistent constitutional rule has been that a court has no power to adjudicate a personal claim or obligation unless it has jurisdiction over the person of the defendant. *E.g., Pennoyer v. Neff*, 95 U.S. 714 (1878); *Vanderbilt v. Vanderbilt*, 354 U.S. 416, 418 (1957)."
>
> *Zenith Radio Corp. v. Hazeltine, supra*, 395 U.S. at 110.

The Court went on to state that Hazeltine Corporation might be bound by the judgment on principles of *res judicata* if it were shown that it in fact controlled the litigation on behalf of HRI, but that claim of *res judicata* could only be finally adjudicated against Hazeltine Corporation in a court which had jurisdiction over that company. *Id.* at 111.

Other circuits have correctly applied these principles in holding that relief may not be granted against a nonparty. *Panther Pumps & Equipment v. Hydrocraft, Inc.*, 566 F.2d 8 (7th Cir. 1977) [corporation not named in an order to show cause why an individual should not be held in contempt could not be substituted in as a defendant before the contempt hearing]; *Commercial Security Bank v. Walker Bank & Trust Co.*, 456 F.2d 1352 (10th Cir. 1972) [the district court lacked jurisdiction to issue an ex parte restraining order preventing a sheriff's sale against the United States which had not been named a party and had not been served with process].

II.

PERMITTING AN ORDINARY CIVIL ACTION TO BE HANDLED AS A SUMMARY PROCEEDING WITHOUT REGARD FOR CRITICAL PROVISIONS OF THE FEDERAL RULES IS SUCH A RADICAL DEPARTURE FROM THE ACCEPTED AND USUAL COURSE OF JUDICIAL PROCEEDINGS THAT THIS COURT SHOULD EXERCISE ITS POWER OF SUPERVISION

The Court should hear this case because the published opinion of the Ninth Circuit promulgates the erroneous and dangerous holding that summary proceedings may be used in lieu of normal plenary trials of civil disputes when they are useful to the purposes of securities receiverships and thereby "avoid *formalities* which would slow down the resolution of disputes." See appendix pp. A-14 — A-15, n. 9, *infra*. (Emphasis applied.) The "formalities"

referred to are the procedures which are prescribed by the Federal Rules of Civil Procedure. It is unfortunate enough that the opinion in this case states such a doctrine, but the problem is compounded by the Ninth Circuit's primary reliance upon its recent decision in *S.E.C. v. Universal Financial*, 760 F.2d 1034 (9th Cir. 1985) which stated that the distinction between summary and plenary proceedings was of no consequence in that case because the district court had afforded the appellants "virtually all" of the procedural protections which are available in plenary proceedings.

The *Universal Financial* opinion is so different on its facts and so lacking in analysis that it is not valid precedent for denial of the claims in this case. However, the effect of it being cited to justify the use of summary proceedings in this case, is to create what appears to be respectable authority for denying petitioner and others the procedural safeguards of the Federal Rules.

In *S.E.C. v. Universal Financial, supra*, appellants were investors ("Investors") who entered into loan transactions through the services of a number of entities controlled by one Wayne Burton who acted as a mortgage loan broker in arranging secured real estate loans on behalf of Investors with supposedly qualified borrowers. In some of the transactions, Investors received documentation which identified individual Investors as payees of the notes and beneficiaries of the trust deed. In others, Burton purported to borrow funds from Investors and then make larger loans to borrowers, pooling monies from different Investors to fund a single loan. In the latter type of transaction, the participating Investors would take a proportionate fractionalized interest in the loan.

The S.E.C. brought an action against Burton for injunctive and other relief, alleging various securities law violations including the false representation that Investors would receive first trust deeds on borrowers' properties when in fact most Investors received only junior deeds of trust. Burton consented to entry of a permanent injunction and an order for accounting and "anti-dissipation of

assets." The district court appointed a receiver to take control of and manage assets for the benefit of Investors and entered a stay of all proceedings by third parties against defendants, the receiver or receivership property.

The receiver categorized the claims of Investors according to his theories of the legal consequences of the different types of investments. The district court approved a modified proposal of categorization over the objection of Investors but held that the issue of whether Investors had ownership interests in particular notes of the borrowers would be litigated in trials pursuant to the court's summary jurisdiction. At the court's suggestion, counsel for Investors and the receiver "agreed to try" two test cases, and this was done after extensive discovery. The result of these trials was a holding of the district court that Investors in the test cases had ownership interests in their notes and could enforce those interests free of any claim by the receiver. The court then ordered that counsel select an additional ten cases for trial.

At this point, Investors filed motions for an order collaterally estopping the receiver from relitigating issues resolved in the test cases and relieving them from the stay order. The motions were denied, and Investors appealed. The initial contention was that because the district court had established in the test cases that Investors were the unconditional owners of rights conferred by these notes, the court could not summarily adjudicate their claims. They asserted that summary jurisdiction is unconstitutional where an adverse claimant presents a substantial claim that he is the owner and not the receiver.

This contention on appeal was disposed of in one paragraph holding that the distinction between summary and plenary proceedings was of no consequence because the court had afforded Investors "virtually all" of the procedural protections of plenary proceedings including extensive discovery (including depositions) and the right to file numerous briefs and exhibits in the test cases. Also, the court applied the Federal Rules of Civil Procedure and

the Federal Rules of Evidence, and it appears from the opinion that the only elements of a regular civil action which were missing were "a formal complaint and answer." The challenge to summary jurisdiction failed because Investors "cannot explain how the summary proceedings differed from the process they would have received in a plenary suit." *Id.* at 1037.

The differences between *Universal Financial* and this case are striking. In the first place, Investors had agreed to try the test cases within the court's summary jurisdiction and so were not in a position to mount a serious challenge to the procedures employed. Also, Investors as a consequence of their victory in the test cases were actually attempting to utilize a different form of summary disposition by their motion for an order collaterally estopping the receiver from relitigating issues decided in the test cases. Finally, it does appear that the Investors received substantially all of the protections which would have been afforded in a regular civil action.

Here, petitioner never consented to summary proceedings and was justified in assuming that if respondent wished to seriously pursue claims against him, respondent would activate the 1980 action which he had filed. By the time petitioner received notice of the hearing on the disgorgement application, there was no time to engage in discovery, briefing or trial preparation. There was no mechanism such as an answer or motion by which to narrow and define the issues to be addressed in discovery, trial preparation and trial. In short, as to this dispute, there was no compliance with any of the Federal Rules of Civil Procedure. This violates, in particular, the provisions of Rules 1 ["These rules govern the procedure in the United States district courts in all suits of civil nature. . . ."], 2 ["There shall be one form of action to be known as 'civil action.'"] and Rule 4 which commands that a summons be served upon the defendant informing him of the time when he is required to appear and defend.

The actions of the district court affirmed by the Ninth Circuit conflict with the principles stated in the controlling opinion of this

Court, *New Hampshire Fire Ins. Co. v. Scanlon*, 362 U.S. 404 (1960). This opinion, cited to the Ninth Circuit, was relegated to footnote treatment in the opinion below. See appendix p. A-14, n. 9, *infra*. In *Scanlon*, a district director of internal revenue served notice of levy on the City of New York demanding that it pay money alleged to be due from the city to a contractor. The contractor's surety, which had completed the contractor's work due to the contractor's business failure, filed a "petition" in the district court seeking to quash the levy. The petition was dismissed by the district court which held that it did not have jurisdiction to determine the respective rights of the parties in a summary proceeding, and its ruling was upheld in the court of appeals and by this Court, which addressed the issue as follows:

> "Summary trial of controversies over property and property rights is the exception in our method of administering justice. Supplementing the constitutional, statutory, and common-law requirements for the adjudication of cases or controversies, the Federal Rules of Civil Procedure provide the normal course for beginning, conducting, and determining controversies. Rule 1 directs that the Civil Rules shall govern all suits of a civil nature, with certain exceptions stated in Rule 81 none of which is relevant here. Rule 2 directs that 'There shall be one form of action to be known as "civil action."' Rule 3 provides that 'A civil action is commenced by filing a complaint with the court.' Rule 56 sets forth an expeditious motion procedure for summary judgment *in an ordinary, plenary civil action*. Other rules set out in detail the manner, time, form and kinds of process, service, pleadings, objections, defenses, counterclaims and many other important guides and requirements for plenary civil trials. The very purpose of summary rather than plenary trials is to escape some or most of these trial procedures.

> Summary trials, as is pointed out in the petitioner's brief, may be conducted without formal pleadings, on short notice, without summons and complaints, generally on affidavits, and sometimes even ex parte. Such summary trials, it has been said, were practically unknown to the English common law and it may be added that they have had little acceptance in this country. In the absence of express statutory authorization, courts have been extremely reluctant to allow proceedings more summary than the full court trial at common law."
>
> *New Hampshire Fire Ins. Co. v. Scanlon, supra*, 362 U.S. at 406-407.

Apart from express statutory authorization, which is not present here, the only other situations in which summary proceedings are proper are those in which courts have determined ownership of property in their possession, where "for illustration, such a proceeding was ancillary to a pending action or where property was held in the custody of court officers, subject to court orders and court discipline." *New Hampshire Fire Ins. Co. v. Scanlon, supra*, 362 U.S. at 409-410. Justification for summary proceedings cannot be found in this narrow exception. The proceedings against petitioner were not ancillary to the main action because he was not a party to it. They were simply tacked on. Also, as the Ninth Circuit correctly determined, there was no *in rem* jurisdiction over petitioner's Ramapo shares or Ramapo's PSI shares. See appendix p. A-7, n. 5, *infra*. In the words of this Court, this was simply "an everyday, garden-variety controversy that regular, normal court proceedings are designed to take care of." *Id.* at 410.

The predictable result of dispensing with the Federal Rules of Civil Procedure was the deprivation of petitioner's rights to due process of law. As Mr. Justice Jackson wrote for the Court:

> "Many controversies have raged about the cryptic and abstract words of the Due Process Clause but there can be no doubt that at a minimum they require that deprivation of life, liberty or property by adjudication be preceded by notice and opportunity for hearing appropriate to the nature of the case."
>
> *Mullane v. Central Hanover Bank & Trust Co.*, 339 U.S. 306, 313 (1950).

What was appropriate to the nature of this case was the treatment afforded to the usual civil action including pleadings for identification of issues, discovery, time for pretrial proceedings, trial preparation and a full trial on the merits. Here, after the disgorgement application had lain dormant for nearly three years, and a plenary action seeking the same relief was commenced, petitioner was given 19 days notice by mail of a hearing which resulted in the taking of his property.

The Ninth Circuit opinion makes much of petitioner's supposed inaction and his ability to have filed a responsive pleading, initiated discovery, sought a continuance of the hearing and presented evidence. Yet apart from repeated references to its *Universal Financial* opinion, no authority was presented that it is a defendant's duty to properly bring himself before the court and undertake the burden and expense of defending against a proceeding which had not been pursued.

The serious error expressed in the Ninth Circuit opinion below and in *S.E.C. v. Universal Financial, supra*, will inevitably lead to further neglect of the rights conferred upon litigants under the Federal Rules of Civil Procedure. The temptation to deny these rights will be especially strong in cases like this where a receiver is attempting to take property for the benefit of defrauded persons. In such cases a perception of the receiver's generally beneficent stewardship will make it easy for courts to use summary

proceedings to "reduce litigation costs to the receivership" and "avoid formalities that would slow down the resolution of disputes." See appendix p. A-14, n. 9, *infra*.

CONCLUSION

For these various reasons, this petition for certiorari should be granted.

Respectfully submitted,

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APPENDICES

UNITED STATES COURT OF APPEALS

FOR THE NINTH CIRCUIT

SECURITIES AND EXCHANGE COMMISSION, Plaintiff, v. WALTER WENCKE, et al., Defendants.	No. 83-6469 OPINION
THEODORE deLUSIGNAN, Movant-Appellant, v. R. N. GOULD, Receiver-Trustee, Appellee.	

Appeal from the United States District Court
for the Southern District of California
Hon. G. Thompson, Jr., District Judge, Presiding
Argued and Submitted September 4, 1984 - Los Angeles, California
Decided February 19, 1986

BEFORE: WALLACE, FLETCHER, and REINHARDT, Circuit Judges.

FLETCHER, Circuit Judge:

Theodore deLusignan appeals from a post-judgment order by the district court requiring Ramapo Corporation ("Ramapo"), in which he is a 25% stockholder, to disgorge 401,351 shares of Portsmouth Square, Inc. ("PSI") and the profits it derived from those shares. The district court issued its order following judgment in a securities fraud action brought by the Securities and Exchange Commission (SEC) against Walter Wencke, who had diverted funds from several public companies and funneled them through Ramapo to acquire the PSI shares. DeLusignan contends that in entering its disgorgement order, the district court exceeded its jurisdiction, violated the Federal Rules of Civil Procedure, and deprived both him and Ramapo of due process. We find these claims to be without merit, and affirm.

FACTUAL BACKGROUND

A. DeLusignan's Acquisition of His Ramapo Stock

PSI was incorporated in 1967 as a vehicle for investors to purchase a substantial interest in Justice Investors, a partnership that owned the Holiday Inn at 750 Kearny Street in San Francisco. In 1972, PSI was experiencing severe financial problems. All of its subsidiaries were losing money, and PSI was on the verge of bankruptcy. In May, 1972, deLusignan, president of PSI, responded to Walter Wencke's advertisement in the Wall Street Journal offering assistance to financially distressed companies.

Wencke proposed a financial aid arrangement to deLusignan and PSI's board of directors, under which Ramapo, a Delaware corporation created by Wencke and entirely owned by the Hansa Trust, a Wencke-family trust, would give PSI $10,000 in cash, assume $338,193 of PSI's liabilities, and provide assistance to PSI in negotiations to extend a $1.2 million obligation for which PSI was in default. In return, PSI would issue Ramapo its remaining authorized and unissued stock, which amounted to 401,351 shares, or a 53.5% controlling interest in the corporation. Wencke also offered to employ deLusignan as an officer of Ramapo, PSI, or

one of their subsidiaries, and to transfer 25 of Ramapo's 100 shares to deLusignan. The PSI board ratified the terms of the stock transfer to Ramapo, and approved deLusignan's proposed employment contract and the transfer to him of the 25 Ramapo shares. Shortly thereafter, Wencke and the other Ramapo shareholder, Paul Potter,[1] approved an employment contract on behalf of Ramapo with deLusignan, and the Hansa Trust made a "gift" to deLusignan of 25 Ramapo shares "in order that [he] would feel part of the [Ramapo] Company." DeLusignan served as president of PSI for the next five years, until 1977.

PSI's transaction with Ramapo enabled PSI to divest itself of unprofitable subsidiaries and to improve its net worth from a negative $323,121 to a positive $25,072. PSI is currently a prosperous, dividend-paying corporation with its shares valued at $6 to $7. DeLusignan contends that PSI's recovery was due in large part to his performance as president. He maintains that by 1977, PSI's hotel property was worth over $50 million, and that prior to the district court's disgorgement order from which he appeals, his Ramapo shares were worth about $2.6 million.

B. The Underlying Securities Fraud Action Against Wencke

In 1976, the SEC brought the underlying securities fraud action against Wencke, his wife, three other individuals, and twenty-five trust and corporate defendants controlled by Wencke and his associates. *See SEC v. Wencke*, 622 F.2d 1363, 1366 (9th Cir. 1980). Wencke was alleged to have violated state and federal law and breached his fiduciary duties by diverting assets and monies from companies and entities he controlled, including Time-Lenders, Inc. ("Time"), Sun Fruit, Ltd. ("Sun Fruit"), Santa Fe Financial Corporation ("Santa Fe"), and their subsidiaries, and using these funds for his personal benefit and profit. DeLusignan, Ramapo, and the Hansa Trust were not parties in the underlying action.

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[1] Potter, who was a named defendant in the underlying securities fraud action against Wencke, held 15 shares in Ramapo.

In March, 1977, the district court entered its final judgment. It permanently enjoined Wencke and the other defendants from further securities activity and ordered Wencke to disgorge all assets or monies that he had taken directly or indirectly. The court appointed R. N. Gould as receiver of Time, Sun Fruit, and Santa Fe. Gould was authorized to assume possession and control over all these companies' assets, to operate them on an ongoing basis, to hire attorneys and accountants to audit and investigate their financial condition and transactions, to resist all actions and claims brought against them, to prosecute all claims they had, and to manage and conserve their assets for the benefit of their defrauded investors until the extent of the receivership estate could be determined. *See id.* at 1366-67.

In November, 1977, the district court specifically appointed the Receiver as voting trustee of the 60 shares of Ramapo owned by Wencke or the Hansa Trust.[2] In March, 1979, the court entered an order directing the Receiver and his counsel to identify and trace all assets and monies that Wencke and those in concert with him had looted from Time, Sun Fruit, Santa Fe, or their subsidiaries, as well as ill-gotten gains derived from those assets, and to initiate disgorgement proceedings to recover those assets and ill-gotten gains. The Receiver has brought six applications for disgorgement.

C. The Disgorgement Proceedings Against DeLusignan and Ramapo

In November, 1980, the Receiver filed two virtually identical pleadings in the district court. First, he filed his Application Number 4 in Disgorgement as a post-judgment pleading in the securities fraud action against Wencke. It was directed at deLusignan, Ramapo, Wencke, the Hansa Trust, and several other individuals and entities, and sought disgorgement of Ramapo's

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[2] By early 1979, Paul Potter had quitclaimed his 15 shares of Ramapo to the Receiver as part of a compromise, leaving the Receiver with 75 Ramapo shares. DeLusignan held the other 25.

corporate charter, the 60 Ramapo shares held by the Hansa Trust, and the 25 shares held by deLusignan. Second, the Receiver filed a complaint initiating a completely separate and independent action against deLusignan, Ramapo, and the Hansa Trust seeking disgorgement of Ramapo's corporate charter and certificates and a declaration imposing a constructive trust over the three defendants' Ramapo holdings. The Receiver amended this complaint in 1982 and deleted Ramapo as a defendant, but the amended complaint still sought disgorgement of deLusignan's 25 Ramapo shares.

The Receiver's disgorgement application was served on Ramapo and the Hansa Trust in January, 1981, and on deLusignan in April, 1981. No summonses were served with the disgorgement application. In November, 1983, deLusignan was served with a summons and the complaint in the separate action filed by the Receiver in 1980.

Following service of the Receiver's disgorgement application upon deLusignan, two years and four months passed without any action being taken on the application. However, deLusignan was deposed in connection with his dealings with Wencke in April, 1981 and again in June, 1981. On August 19, 1983, deLusignan was served with another copy of the disgorgement application, a set of supporting documents, and a notice of hearing to be held on the application before the magistrate/special master nineteen days later.

On September 2, 1983, deLusignan filed an objection to the scheduled hearing, claiming that the district court lacked personal jurisdiction over him, and that permitting the Receiver to proceed against him with the disgorgement application would violate his due process rights. The magistrate/special master conducted an evidentiary hearing on the disgorgement application, at which deLusignan's counsel made only a "special appearance" and did

not present evidence or question witnesses.[3] The evidence indicated that Wencke had diverted at least $89,000 from Time, Santa Fe, and their subsidiaries, and had advanced these funds to Ramapo to acquire a majority interest in PSI and to provide operating funds for PSI. At the conclusion of the hearing, the magistrate indicated that he was prepared to find that Ramapo's assets, specifically its PSI shares and the profits it had derived from them, constituted "ill-gotten gains and as such are subject to disgorgement."

Counsel for the Receiver was directed to prepare findings of fact, conclusions of law, and recommendations. The magistrate adopted these findings and recommendations as drafted, and lodged them with the district court on October 7, 1983. The magistrate recommended that Ramapo be deemed a constructive trustee for the benefit of Time's and Santa Fe's defrauded shareholders, and that it be required to disgorge its PSI shares and the profits it had derived from them. Under the magistrate's recommendations, deLusignan was not required to relinquish any of his Ramapo

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[3] We cannot understand why DeLusignan's counsel made a "special appearance" to raise his client's jurisdictional and procedural objections before both the magistrate/special master and the district court. Federal Rule of Civil Procedure 12 abolished the distinction between general and special appearances when the Federal Rules were adopted in 1938. *See, e.g., Republic International Corp. v. Amco Engineers, Inc.*, 516 F.2d 161, 165 (9th Cir. 1975) ("Special appearances to challenge jurisdiction are no longer required in federal courts."); *Hays v. United Fireworks Manufacturing Co.*, 420 F.2d 836, 844 n. 10 (9th Cir. 1969) (same); *Dragor Shipping Corp. v. Union Tank Car Co.*, 378 F.2d 241, 243 n. 2 (9th Cir. 1967); *Martens v. Winder*, 341 F.2d 197, 200 (9th Cir.) ("Rule 12 . . . eliminat[es] the distinction between general and special appearances."), *cert. denied*, 382 U.S. 937 (1965); 5 Wright and Miller, *Federal Practice and Procedure* § 1344, at 522 (1969) ("[T]echnical distinctions between general and special appearances have been abolished and no end is accomplished by retaining the terms in federal practice."). Thus, deLusignan's counsel could have presented evidence, questioned witnesses, or raised arguments on the merits of the disgorgement proceeding without sacrificing his client's right to challenge the court's jurisdiction.

shares, although Ramapo's disgorgement of its PSI holdings and accrued profits made those shares virtually worthless.[4]

On the same day, the Receiver moved the district court for adoption of the magistrate's findings, conclusions, and recommendations. On October 17, 1983, deLusignan filed a notice of special appearance in the district court and filed objections to the magistrate's findings and recommendations. He objected on the grounds that the court lacked jurisdiction over him and that the conduct of the disgorgement proceedings violated the Federal Rules of Civil Procedure and due process.[5] DeLusignan did not

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[4] DeLusignan now contends that this decision by the magistrate to order disgorgement *by Ramapo of its PSI holdings*, rather than disgorgement *by deLusignan and the Hansa Trust of their Ramapo shares* represented a "dramatic[ ]" shift in the nature of the disgorgement proceedings, and therefore unjustly "surprised" him and Ramapo. However, the Receiver's original disgorgement application listed Ramapo along with deLusignan and the Hansa Trust as "parties subject to disgorgement." Moreover, deLusignan never raised this claim at the district court, and never sought a continuance so that he could respond to this change in the Receiver's disgorgement strategy during the seventeen days between the issuance of the magistrate's findings, conclusions, and recommendations, and the district court's October 24, 1983 hearing on the Receiver's motion to adopt those recommendations.

[5] The Receiver contends that even if the district court did not have *personal* jurisdiction over deLusignan, it had *in rem* jurisdiction over Ramapo and its PSI shares, which entitled it to order Ramapo to disgorge those shares. Yet the district court made no specific finding that Ramapo's PSI shares were physically located within California, which would have been required for it to exercise *in rem* jurisdiction over those shares. *See* 4 Wright and Miller, *Federal Practice and Procedure* § 1071, at 273-74 (1969). Moreover, although the district court had acquired jurisdiction over all Wencke's assets in order to satisfy the claims against him, at the time of the district court's judgment, Wencke owned only 75 of Ramapo's 100 shares. Ramapo and deLusignan were not parties to the securities fraud action against Wencke, and therefore, deLusignan's 25 Ramapo shares and the Ramapo corporation itself were not already within the district court's jurisdiction at the time the Receiver filed his disgorgement application. We need not decide the precise extent of the district court's *in rem* jurisdiction, however, in light of our conclusion that the district court had personal jurisdiction over both Ramapo and deLusignan. *See* Section B, *infra*.

object to any of the specific findings of fact or conclusions of law made by the magistrate.

On October 24, 1983, the district court held a hearing on the Receiver's motion to adopt the magistrate's recommendations and on deLusignan's objections to those recommendations. On November 7, 1983, the court rejected deLusignan's claims, adopted the magistrate's findings, conclusions, and recommendations, and ordered Ramapo to disgorge its PSI holdings and the profits it had acquired from PSI. It is from this order that deLusignan appeals.

ANALYSIS

Since the district court did not order deLusignan to disgorge his Ramapo shares or any other property, but only ordered Ramapo to disgorge its PSI shares and profits, deLusignan's claims are based entirely upon the decrease in the value of his Ramapo shares resulting from Ramapo's disgorgement. As a result, the challenges deLusignan raises to the district court's disgorgement order and proceedings are essentially challenges on behalf of Ramapo as well as himself.

DeLusignan contends that the district court improperly employed summary, rather than plenary, proceedings when it determined that Ramapo was required to disgorge its PSI holdings, and that in the process, the district court exceeded its jurisdiction, violated the Federal Rules of Civil Procedure, and denied him and Ramapo due process. DeLusignan also maintains that the district court provided him and Ramapo with inadequate preparation time to respond to the Receiver's disgorgement application and to the magistrate's recommendation that Ramapo's PSI holdings, rather than the shares of Ramapo held by deLusignan and the Receiver, be disgorged. We find these claims to be without merit.

A. DeLusignan's Standing to Appeal

Before addressing the merits of deLusignan's claims, we must first determine whether he has standing to bring this appeal. The Receiver contends that deLusignan lacks standing to challenge the district court's disgorgement order, because the order was directed at Ramapo, and deLusignan never formally moved to intervene as a party in district court. We do not agree.

Although persons who were not parties of record before the district court usually may not appeal that court's orders or judgment, we have allowed such persons to bring appeals in cases where: (1) they participated in the district court proceedings, and (2) the equities weigh in favor of hearing the appeal. *In re Proceedings Before Federal Grand Jury (Conforte)*, 643 F.2d 641, 643 (9th Cir. 1981). We have specifically authorized nonparty creditors to appeal a district court's post-judgment order regarding an SEC-initiated receivership, where, as in the present case, they did not formally seek to intervene in the trial court, but nevertheless participated in the district court's proceedings and had "a legitimate interest" in the outcome of the appeal. *SEC v. Lincoln Thrift Association*, 577 F.2d 600, 602-03 (9th Cir. 1978) (citing *West v. Radio-Keith-Orpheum Corp.*, 70 F.2d 621, 623-24 (2d Cir. 1934)); *see SEC v. An-Car Oil Co.*, 604 F.2d 114, 119 & n.4 (1st Cir. 1979). Moreover, other courts have indicated that the equities supporting a nonparty's right to appeal an order relating to a receivership are especially significant where the receiver has haled the nonparty into the proceeding against his will, and then has attempted to thwart the nonparty's right to appeal by arguing that he lacks standing. *See West*, 70 F.2d at 623-24, *quoted in Lincoln Thrift*, 577 F.2d at 603; *An-Car Oil Co.*, 604 F.2d at 119 n.4; *see also In re Proceedings*, 643 F.2d at 643 n.2.

In the present case, it is undisputed that deLusignan participated in the district court's proceedings. The Receiver haled deLusignan and Ramapo into district court despite deLusignan's objections. DeLusignan made a special appearance and raised all the jurisdic-

tional, procedural, and due process claims that he is now raising on appeal. Throughout its proceedings, the district court treated deLusignan as if he were a party, accepting his briefs, asking him questions at hearings, and offering him the opportunity to cross-examine witnesses -- even after the object of the disgorgement proceeding changed from deLusignan's Ramapo shares to Ramapo's PSI holdings. Because it was clear at the time that the value of deLusignan's Ramapo holdings would be substantially diminished by Ramapo's disgorgement of its PSI stock, and because Ramapo did not adequately represent deLusignan's interest in the district court's proceedings, deLusignan would have been entitled to intervene in those proceedings as of right under Federal Rule 24(a). *See* Fed. R. Civ. P. 24(a)(2);[6] *see also County of Fresno v. Andrus*, 622 F.2d 436, 438 (9th Cir. 1980). The fact that the district court allowed and encouraged deLusignan to participate fully in its proceedings even after he was no longer a target of disgorgement suggests that it perceived him as an intervenor.[7] For all these reasons, we conclude that deLusignan "participated" in the district court's disgorgement proceedings directed at Ramapo.

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[6] We conclude that the disgorgement of Ramapo's PSI shares would "as a practical matter *impair* . . . [deLusignan's] ability to protect [his] interest" in the value of his Ramapo shares. Fed. R. Civ. P. 24(a)(2) (emphasis added). This is not inconsistent with our conclusion, *see infra*, that deLusignan may still be entitled to recover damages for the lost value of his Ramapo shares or for the value of his services to Ramapo and PSI. It merely reflects that deLusignan will be required to pursue litigation to recover the lost value of his Ramapo holdings, and that he may not succeed in that litigation.

[7] At least two circuit courts have held that if trial courts treat potential intervenors essentially as parties during proceedings, they should be treated as intervenors at the appellate level as well, even if they have not complied with the formal requirements of Rule 24. *See International Marine Towing, Inc. v. Southern Leasing Partners, Ltd.*, 722 F.2d 126, 128-29 (5th Cir. 1983), *cert. denied*, 105 S.Ct. 94 (1984); *In re Beef Industry Antitrust Litigation*, 589 F.2d 786, 789 (5th Cir. 1979); *Roach v. Churchman*, 457 F.2d 1101, 1104 (8th Cir. 1972); *see also Lincoln Thrift*, 577 F.2d at 603. Because we conclude that deLusignan has satisfied the two requirements to bring an appeal delineated in *In re Proceedings*, we need not make such a ruling in the present case.

Moreover, we conclude that the equities weigh in favor of hearing deLusignan's appeal. The Receiver chose to hale deLusignan and Ramapo into the district court, and should therefore not be permitted to thwart deLusignan's appeal based on lack of standing, especially when deLusignan could have qualified to intervene as of right under Rule 24(a) had he formally applied. *See An-Car Oil Co.*, 604 F.2d at 119 n.4. Since the target of disgorgement changed near the end of the disgorgement proceedings, there may have been confusion as to who were the parties of record. Furthermore, the disgorgement proceedings were summary in nature, and the district court did not require the parties to file formal complaints or answers, or to serve summonses. *See SEC v. Universal Financial*, 760 F.2d 1034, 1037 (9th Cir. 1985) (per curiam). Thus, it would have been reasonable for deLusignan to believe that he did not need to file a formal motion to intervene. The Receiver and other parties were aware of deLusignan's participation and had a full opportunity to respond to his arguments in the district court proceedings, and to develop any record necessary to respond to those arguments. As a result, it would be both inconsistent and inequitable for this court to refuse to hear deLusignan's appeal based simply upon his failure to file a formal motion to intervene. It would have been better had deLusignan moved to intervene. *In re Proceedings*, 643 F.2d at 643; *Lincoln Thrift*, 577 F.2d at 6703. Nevertheless, because deLusignan participated in the district court's disgorgement proceedings, and because the equities weigh in favor of hearing his appeal, we conclude that deLusignan has standing to bring his appeal.

B. DeLusignan's Challenges to the Disgorgement Proceedings

DeLusignan raises two sets of challenges to the district court's disgorgement order and proceedings. First, he challenges the district court's employment of summary, post-judgment proceedings when it ordered disgorgement of Ramapo's PSI holdings, rather than requiring the Receiver to pursue the separate, plenary action the Receiver had initiated against deLusignan, Ramapo, and the Hansa Trust in 1980. Second, deLusignan contends that

the district court's disgorgement proceedings violated due process, because he and Ramapo were required to respond to the Receiver's disgorgement application within only nineteen days, and because the nature of the disgorgement sought by the Receiver was altered at the last minute.

1. Challenge to the Use of Summary Proceedings

DeLusignan maintains that if the Receiver wanted to seek disgorgement of Ramapo's PSI holdings, he should have been required to pursue the independent action he filed in 1980, and should not have been permitted to circumvent the requirements of civil procedure and due process by seeking disgorgement in summary post-judgment proceedings. DeLusignan contends that: (1) the district court lacked jurisdiction to enter its disgorgement order against him and Ramapo, since neither of them had been a party to the underlying securities fraud action against Wencke or was bound by the default judgment in that action; (2) the disgorgement proceedings violated the Federal Rules of Civil Procedure, since they were conducted without the filing of a formal complaint or answers, and since the disgorgement application was served on deLusignan and Ramapo without summonses; and (3) the disgorgement proceedings violated due process, since they were summary in nature and did not provide full-scale procedural protections.

We cannot accept deLusignan's contentions. We rejected like claims either implicitly or explicitly in a recent case, *SEC v. Universal Financial*, 760 F.2d at 1034. *Universal Financial* arose out of a securities fraud action brought by the SEC against a mortgage loan broker who had misrepresented to various investors the nature of the security interests he sold them; the district court appointed a receiver to manage the broker's assets for the benefit of his investors. *Id.* at 1036. The receiver attempted to categorize the various investors' ownership interests in the promissory notes and deeds of trust held in the receivership, and the district court ruled that the extent of these ownership interests could be determined in

trials pursuant to its summary jurisdiction. *Id.* at 1036-37. A set of investors, who had not been parties to the underlying securities fraud action, challenged the district court's jurisdiction to adjudicate their claims in summary proceedings, contending that "summary jurisdiction is unconstitutional where an adverse claimant presents a substantial claim that he, rather than a receiver . . . is the owner of [a property interest or right held within a receivership]." *Id.*

We rejected the investors' contention that district courts are flatly prohibited from adjudicating in summary post-judgment proceedings the claims of nonparties to property claimed by securities receivers. *See id.* We indicated that to determine the adequacy of a summary proceeding in a given case, courts must focus not on the *form* of the proceedings, but on their *substance*: in *Universal Financial*, for example, "the distinction between summary and plenary proceedings was of no consequence . . . because the district court afforded [the nonparties challenging its jurisdiction] virtually all of the procedural protections which would have been available in plenary proceedings." *Id.* (citation omitted); *see In re Reading Co.*, 711 F.2d 509, 516-17 (3d Cir. 1983) (citation omitted). We did not accept the contention that the lack of a formal complaint and answer prevented the district court from exercising its jurisdiction and resolving the dispute, because the parties challenging jurisdiction had notice concerning the nature of the proceedings, were permitted extensive discovery, including the taking of depositions, and were permitted to file briefs and exhibits with the district court, and because, except for dispensing with the filing of a complaint and answer, the district court applied

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[8] In *Universal Financial*, the district court had conducted two "test cases" in which various investors had litigated their ownership interests to promissory notes held by the receiver, and had held that the investors in both cases had valid ownership interests in the notes. *See* 760 F.2d at 1037. The district court then ordered counsel to select ten additional test cases for trial, and the investors filed the objections that became the basis of the appeal.

the Federal Rules of Evidence and Civil Procedure.[9] *See Universal Financial*, 760 F.2d at 1037.

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[9] DeLusignan contends that the Supreme Court's decision in *New Hampshire Fire Insurance Co. v. Scanlon*, 362 U.S. 404 (1960), flatly precludes the use of summary, rather than plenary, proceedings in this case, since there is no express statutory authorization for the use of such procedures in the present context. We do not read *Scanlon* so broadly.

The Supreme Court said in *Scanlon* that "[i]n the absence of express statutory authorization, courts have been extremely reluctant to allow proceedings more summary than the full court trial at common law." *Id.* at 407 (citations omitted). We agree that courts should be "reluctant" to authorize the use of summary proceedings unless there is a strong reason for doing so. In many cases, the use of summary proceedings would deprive parties of a full and fair opportunity to prepare and present their claims and defenses, and therefore, such proceedings cannot be employed. However, under the pragmatic analysis we applied in *Universal Financial*, courts are not flatly barred from employing summary proceedings when parties have been given an opportunity to prepare and present their contentions. The Supreme Court noted in *Scanlon* that there are a wide variety of types of "summary" trials that courts can provide: the term encompasses trials that "may be conducted without formal pleadings, on short notice, without summons and complaints, generally on affidavits, and sometimes even *ex parte*." *Id.* at 406. The Court plainly did not announce a blanket rule covering all these types of summary trials. *See id.* at 406-10.

Some courts have interpreted *Scanlon* to permit courts to employ summary procedures "for adjudication of . . . matter[s] ancillary to a pending judicial proceeding," such as the present dispute over disgorgement. *See e.g., Application of Howard*, 325 F.2d 917, 919 (3d Cir. 1963); *see also SEC v. Investors Security Corp.*, 560 F.2d 561, 567 (3d Cir. 1977) (holding that when "receiver acted within the powers delegated by the [trial] court to accomplish ends sought by the underlying action, [such as] protect[ing defrauded] investors and creditors, the district court had jurisdiction over the proceeding . . . as an ancillary matter"); *Tcherepnin v. Franz*, 485 F.2d 1251, 1255-56 (7th Cir. 1973) (same), *cert. denied*, 415 U.S. 918 (1974); *Esbitt v. Dutch-American Mercantile Corp.*, 335 F.2d 141, 142 (2d Cir. 1964) (same). Our decision in *Universal Financial*, although not referring specifically to *Scanlon*, is consistent with these cases.

Our court, like many others, has recognized that as part of courts' equitable powers under the Securities Acts of 1933 and 1934, it may impose receiverships in securities fraud actions to prevent further dissipation of defrauded investors' assets. *SEC v. Wencke*, 622 F.2d at 1369 ("The federal courts have inherent equitable authority to issue a variety of 'ancillary relief' measures in actions brought by the SEC . . . . This circuit has repeatedly approved imposition of a

In light of our decision in *Universal Financial*, deLusignan's jurisdictional and procedural challenges to the disgorgement proceedings must fail. DeLusignan has failed to demonstrate how he and Ramapo were prejudiced by the fact that the disgorgement proceedings were summary in nature, or that they would have been better able to defend their interests in a plenary proceeding. DeLusignan and Ramapo had notice of the disgorgement proceedings directed against them: the Receiver served them with the disgorgement application, naming them as parties subject to disgorgement, over two years before the magistrate and district court held disgorgement hearings. Nothing prevented deLusignan or Ramapo from filing a responsive pleading to the disgorgement

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receivership . . . . [T]he authority derives from the inherent power of a court of equity to fashion effective relief."); *see also Mills v. Electric Auto-Lite Co.*, 396 U.S. 375, 391 (1970) ("[W]e cannot fairly infer from the Securities Exchange Act of 1934 a purpose to circumscribe the courts' power to grant appropriate remedies."); *J.I. Case Co. v. Borak*, 377 U.S. 426, 433 (1964); *Deckert v. Independence Shares Corp.*, 311 U.S. 282, 288 (1940); 3 L. Loss, *Securities Regulation* 1513-14 & n.117, 1805-08, 1828 & n.482 (2d ed. 1961); Farrand, *Ancillary Remedies in SEC Civil Enforcement Suits*, 89 Harv. L. Rev. 1779, 1784-89 (1976). Similarly, courts may require disgorgement of diverted assets in securities fraud actions. *See Manor Nursing*, 458 F.2d at 1104; *see also* Ellsworth, *Disgorgement in Securities Fraud Actions Brought by the SEC*, 1977 Duke L. J. 641; Farrand, *supra*, at 1800-05; 3 L. Loss, *supra*, at 1805-08, 1824-29. No specific statutory provision authorizes the creation of securities receiverships or imposition of a disgorgement remedy; *a fortiori*, no statute authorizes courts to employ summary procedures in actions involving these receiverships.

Yet there are compelling reasons to permit the use of summary post-judgment proceedings in such cases, as long as the requirements of *Universal Financial* are satisfied. The use of such proceedings enables a receiver to consolidate all litigation concerning his receivership in a single district court and before a single district judge, and to avoid formalities that would slow down the resolution of disputes. This promotes judicial efficiency and reduces litigation costs to the receivership. *See Smith v. American Industrial Research Corp.*, 665 F.2d 397, 399 (1st Cir. 1981) ("Sound judicial management requires that the equities and priorities among claimants to receivership assets normally be determined in [a single] receivership proceeding . . . ."). The primary purpose of allowing courts to establish receiverships in securities fraud actions is to prevent further dissipation of the assets of the defrauded investors; the use of summary post-judgment proceedings helps to effectuate this.

application or seeking discovery at any time between 1981 and the issuance of the district court's disgorgement order in November, 1983. DeLusignan did nothing during that time on behalf of himself or Ramapo.

Although deLusignan was deposed for a total of five days in 1977 and 1981, nothing in the record indicates that he *sought* any discovery on behalf of himself or Ramapo. DeLusignan and Ramapo were given the opportunity to introduce evidence and to call and cross-examine witnesses in the hearings before the magistrate and district court. Yet deLusignan's counsel merely entered a "special appearance". Even though the target of disgorgement sought by the Receiver appears to have changed late in the process, deLusignan and Ramapo had seventeen days between the issuance of the magistrate's recommendations, suggesting disgorgement of Ramapo's PSI holdings, and the district court's hearing on those recommendations. DeLusignan made no objections on the merits and did not request additional time to do so.

Given our decision in *Universal Financial* and given "all of the procedural protections" available to deLusignan and Ramapo in the district court's disgorgement proceedings, *see Universal Financial*, 760 F.2d at 1037, we reject deLusignan's contentions that the use of summary proceedings and the lack of a formal complaint, answer, and summonses voids the district court's disgorgement order.

2. Due Process Challenges

DeLusignan contends that his and Ramapo's due process rights were violated, because they were given only nineteen days to prepare for the disgorgement hearing before the magistrate, and because the relief sought by the Receiver was altered at a late stage of the district court proceedings. We reject these claims. DeLusignan and Ramapo were served with the Receiver's disgorgement application well over two years before the Receiver

noticed a hearing on the matter. DeLusignan and Ramapo never sought a continuance even after the hearing on the disgorgement application had been noticed.

Nor can deLusignan and Ramapo contend that they were "surprised" by the change in the nature of the disgorgement sought by the Receiver. The Receiver's original disgorgement application listed Ramapo, as well as deLusignan, as a "party subject to disgorgement." Thus, deLusignan cannot claim that the Receiver's attempt to obtain disgorgement of Ramapo's PSI holdings was unexpected. As noted above, the magistrate issued his recommendation that Ramapo disgorge its PSI holdings on October 7, 1983. During the seventeen days prior to the district court's hearing on that recommendation, and the thirty-one days before the district court adopted the recommendation, deLusignan never sought a continuance so that he might respond to the different form of relief allegedly being sought.

Thus, since deLusignan and Ramapo should have been aware for over two years that the Receiver might seek disgorgement by Ramapo of its PSI holdings, and since deLusignan had ample opportunity to request additional preparation time if he had been surprised by the approaching hearing date or the magistrate's recommendation, we conclude that deLusignan's and Ramapo's due process rights were not violated. Because deLusignan's challenges to the district court's order and proceedings are without merit, we affirm the disgorgement of Ramapo's PSI holdings.[10]

---

[10] Since the district court's disgorgement order is directed exclusively at Ramapo, the district court's decision and our affirmance do not preclude deLusignan from asserting any claims he may have on his own behalf based on his employment agreement with Wencke, possible fraud or misrepresentation by Wencke, the "quantum meruit" value of the services he provided between 1972 and 1977 to Ramapo and PSI, and his rights as a minority shareholder of Ramapo. The evidence in the record supports the district court's finding that Ramapo purchased its PSI holdings with funds diverted from Time, Santa Fe, and their subsidiaries. Thus, the district court's order requiring Ramapo to disgorge its PSI shares was proper.

AFFIRMED.

As it currently stands, however, the record does not support a finding that deLusignan conspired or cooperated with Wencke in his fraudulent activities, and does not support any other finding that would require disgorgement by deLusignan of his Ramapo shares. No such finding was necessary to the district court's disgorgement order. We recognize that the findings drafted by the Receiver's counsel and ultimately adopted by the district court include a finding that deLusignan knowingly participated in Wencke's securities fraud. However, since that finding is not essential or even relevant to the district court's disgorgement order directed at Ramapo, which is the subject of this appeal, the lack of factual support for it does not necessitate reversal.

B-1

UNITED STATES DISTRICT COURT

SOUTHERN DISTRICT OF CALIFORNIA

SECURITIES AND EXCHANGE COMMISSION, Plaintiff, v. WALTER WENCKE, et al., Defendants.	Civil Action No. 76-0783-GT(M) ORDER ADOPTING FINDINGS OF FACT, CONCLUSIONS OF LAW AND RECOMMENDATIONS RE RECEIVER'S APPLICATION NO. *4* IN DISGORGEMENT

This cause came to be heard before this Court on October 24, 1983 upon the Receiver's Motion for an Order Adopting the Findings of Fact, Conclusions of Law, and Recommendations re Receiver's Application No. *4* in Disgorgement ("Findings") lodged with the Clerk of this Court on October 7, 1983 by United States Magistrate and Special Master, Harry R. McCue. A true and correct copy of said Findings are attached hereto as Exhibit "A" and herein incorporated by reference. Appearing on behalf of the Receiver, R. N. Gould, were Michael S. Polan and Patricia I. James of the Law Firm of Alex A. Harper. Richard B. Munks of Procopio, Cory, Hargreaves and Savitch appeared specially on behalf of Theodore A. deLusignan.

It appearing to the Court that it has jurisdiction over the parties and the subject matter hereof, and the Court having reviewed the Findings, Conclusions and Recommendations of Magistrate McCue, and having considered the original Findings of Fact and Conclusions of Law and Final Judgment entered herein, as well as the Order Imposing Trust and Appointing Trustee and the Order Authorizing Disgorgement, and having considered all pleadings,

affidvits and documents filed herein, including the pleadings filed on behalf of Theodore A. deLusignan, and good cause appearing therefor, the Court being fully advised in the premises;

The Court finds that it has jurisdiction to adopt and order the Findings, Conclusions and Recommendations set forth by Magistrate McCue and that the adoption and order thereof does not deprive Mr. deLusignan of due process of law.

WHEREFORE, IT IS ORDERED, that the Findings of Fact, Conclusions of Law and Recommendations re Application No. *4* are hereby adopted by this Court in their entirety.

IT IS FURTHER ORDERED that the 401,351 shares of Portsmouth Square, Inc. held of record by The Ramapo Corporation and the assets and profits of The Ramapo Corporation derived from said 401,351 shares of Portsmouth Square are hereby disgorged to the Receiver, R. N. Gould, in trust for the benefit of the innocent public shareholders of Time-Lenders, Inc. and Santa Fe Financial Corporation.

IT IS FURTHER ORDERED that the Receiver continue in his disgorgement proceedings consistent with the Findings of Fact and Conclusions of Law adopted herein.

DATED November 7, 1983

Gordon Thompson Jr

GORDON THOMPSON, JR., United States District Court Judge

UNITED STATES DISTRICT COURT

SOUTHERN DISTRICT OF CALIFORNIA

SECURITIES AND EXCHANGE COMMISSION, Plaintiff, vs. WALTER WENCKE, et al., Defendants.	Civil Action No. 76-0783-GT(M) FINDINGS OF FACT, CONCLUSIONS OF LAW AND RECOMMENDATIONS RE APPLICATION NO. *4*

The Receiver's Application No. *4* in Disgorgement came to be heard before United States Magistrate and Special Master Harry R. McCue on September 7, 1983. Appearing on behalf of the Receiver, R. N. Gould, were Michael S. Polan, Michael G. Zybala and Patricia I. James of the Law Firm of Alex A. Harper. Appearing specially on behalf of Theodore A. deLusignan was Richard B. Munks of Procopio, Cory, Hargreaves and Savitch. Michael Duckor of Duckor & Spradling appeared on behalf of Palmer York and Goerge Croke. The Court noted the Objections to Hearing set forth on behalf of Mr. deLusignan and overruled the same. After a complete hearing which included the testimony of witnesses Virginia W. Simpson and R. N. Gould, the admission of documentary evidence, and the presentation of oral argument, having considered the Final Judgment and the Findings of Fact and Conclusions of Law entered herein, the Receiver's and Trustee's Reports, all other documents on file with the Court, and having reviewed the Application of the Receiver and the supporting Affidavits and Exhibits, and all pleadings, and good cause appearing therefor, this Court makes the following Findings of Fact, Conclusions of Law and Recommendation.

FINDINGS OF FACT

1. On March 7, 1977, this Court entered its Final Judgment of Permanent Injunction, Appointment of Receiver and Special Master and Other Relief ("Final Judgment"). By this Final Judgment, R. N. Gould was appointed Receiver of certain public companies formerly controlled by Walter Wencke, including Time-Lenders, Inc. ("Time") and Santa Fe Financial Corporation ("Santa Fe"). Paragraph VI A(7) of said Final Judgment charged the Receiver with the duty to investigate and prosecute all claims arising from the activities of past management, controlling persons or employees of the receivership entities. Paragraph VI A(10) of the Final Judgment further charged the Receiver with the duty to review all past Securities and Exchange Commission ("Commission") filings and shareholders' reports made by Santa Fe and Time for material misstatements or omissions.

2. Pursuant to Paragraph VI (B)(1) of the Final Judgment, defendant Walter Wencke, his agents and employees were requuired to deliver to the Receiver possession and custody of all funds, securities, property, assets, books and records of the entities in receivership.

3. Paragraph VII of the Final Judgment further required the disgorgement by Walter Wencke of any and all assets or monies taken directly or indirectly from Time-Lenders or Santa Fe, among others, in violation of state or federal law or in breach of fiduciary duty. Said paragraph also required the Special Master to submit a report containing his recommendations on the appropriate manner and amount of disgorgement.

4. On November 4, 1977, this Court entered its Order Imposing Trust and Appointing Trustee which supplemented the Final Judgment herein. By virtue thereof, R. N. Gould was appointed Voting Trustee of the shares of The Ramapo Corporation ("Ramapo") owned by Walter Wencke or his family trust, The Hansa Trust ("Hansa Trust"). At that time, Hansa Trust owned

60% of Ramapo which owns 401,351 shares of and is the majority shareholder of Portsmouth Square, Inc. ("PSI"), a public company with a 49.8% interest in Justice Investors, Ltd., a limited partnership which owns the San Francisco Holiday Inn-Financial District.

5. At the time of Ramapo's incorporation in 1972, Hansa Trust held 100% of its 100 outstanding shares. However, on June 15, 1972, Hansa Trust, pursuant to the directions of Walter Wencke, transferred 25% of its shares in Ramapo to Theodore A. deLusignan ("deLusignan") and 15% to Paul Potter ("Potter"). Pursuant to a Stipulation, Agreement and Order Regarding Dismissal of Actions Against Paul Potter entered herein on December 18, 1979, Potter quitclaimed for no monetary consideration his 15% interest in Ramapo to the Receiver in trust subject to disgorgement for the benefit of Time and Santa Fe.

6. On or about February 1, 1983, this Court approved a Compromise by and between the Receiver/Trustee, R. N. Gould, and Wayne and Wenda Wencke which, among other things, resulted in a resolution of this disgorgement action with respect to their interests individually and by and through Hansa Trust. As a result thereof, Hansa Trust transferred its 60 shares of Ramapo to the Receiver in trust for the benefit of Time and Santa Fe. Said Compromise did not affect any claims or judgments the Receiver maintains against Walter Wencke and allows the Receiver to pursue all claims, including disgorgement, he has or may have againt Walter Wencke. As a result of this settlement, the Receiver presently hold 75% of the outstanding shares of Ramapo in trust.

7. On March 27, 1979, this Court entered its Order Authorizing Disgorgement Proceedings and Granting Injunctive Relief, and Findings. Said Order charged the Receiver and his counsel with the duty to, among other things, identify and trace any and all assets, monies and fruits ("ill-gotten gains") from said assets or monies, wherever located, taken directly or indirectly from Time or Santa Fe or their current or former subsidiaries, by Walter

Wencke and/or those acting in concert with him, in violation of state or federal law or in breach of fiduciary duty. This is the Receiver's fourth application in his efforts to identify and return these "ill-gotten gains" to the public companies from which they were looted.

8. The Court finds that the Receiver's Disgorgement Application was duly noticed and served. On January 19, 1981, service by mail of Application No. *4* was effectuated upon Walter Wencke and the Securities and Exchange Commission. On January 20, 1981 the Application was personally served upon Ramapo, Kentfield Financial, Inc. ("Kentfield") and Hansa Trust. Personal service of Application No. *4* and the supporting Affidavit of Virginia W. Simpson was effectuated upon Theodore deLusignan on April 22, 1981. Service of the Application was also effectuated upon Adele Wencke, Wayne Wencke and Wenda Wencke.

9. On August 19, 1983, Notice of the September 7, 1983 hearing along with the supporting Affidavit of R. N. Gould were served by mail upon Walter Wencke, the Securities and Exchange Commission, Theodore de Lusignan and his attorney, James Granby, and the Receiver, R. N. Gould.

10. In connection with his violations of federal securities laws and other wrongful activities described herein, Walter Wencke, directly and indirectly, used means and instrumentalities of interstate commerce and the United States mails.

11. Santa Fe is a Nevada corporation doing business in San Diego, California and registered with the Commission pursuant to Section 12(g) of the Securities Exchange Act of 1934 ("Exchange Act") [15 U.S.C. §78*l*(g)]. Santa Fe is one of the corporations specifically delineated in the Order Authorizing Disgorgement Proceedings and is subject to the receivership estate established in this action.

12. Time is a California corporation which, at all relevant times hereto, was registered with the Commission pursuant to Section 12(g) of the Exchange Act [15 U.S.C. § 78*l*(g)]. Time is one of the corporations specifically delineated in the Order Authorizing Disgorgement Proceedings and subject to the receivership estate established in this action. Meti, a wholly owned subsidiary of Time, is a Nevada corporation doing business in San Diego, California.

13. At all relevant times, Walter Wencke owned or controlled more than 60% of the outstanding common stock of Santa Fe which, in turn, owned or controlled 100% of the outstanding Class B non-voting common stock of Time. Walter Wencke also owned or controlled 60% of the outstanding Class A voting common stock of Time. Therefore, Walter Wencke, directly or indirectly, owned or controlled 98% of the aggregate outstanding voting and non-voting common stock of Time.

14. At all relevant times, Walter Wencke was the controlling person and President or Chairman of the Board of Santa Fe, Time, Meti, Ramapo and Kentfield.

15. Wencke incorporated Ramapo in Delaware on March 17, 1972. However, Ramapo's business was primarily conducted in San Diego, California. The Court finds that Ramapo was utilized by Wencke merely as a conduit in the diversion of public company monies to Portsmouth Square. Furthermore, Ramapo was created and utilized by Wencke and/or those acting in concert with him, to receive, hide and conceal the ill-gotten gains delineated hereinbelow at Paragraph 15 of the Conclusions of Law. The fraudulent manipulation by Walter Wencke of The Ramapo Corporation's separate corporate existence is best evidenced by the fact that Walter Wencke did not cause Hansa Trust to pay for its share in Ramapo until one and a half years later, in October, 1973.

16. The acts giving rise to Application No. *4* were performed by the persons and parties subject to disgorgement and occurred in

large part in the Southern District of California, and Walter Wencke and the trusts and corporations with whom Walter Wencke transacted business, including Ramapo, maintain offices or are otherwise doing business in the Southern District of California.

17. The acts initially giving rise to this Application were as follows: On May 25, 1972, Santa Fe was issued a check in the amount of $11,000 by Meti for which Meti received in exchange a 90-day promissory note due ninety days subsequent to date of May 25, 1972, in the sum of $11,000 with interest at the rate of eight percent (8%) per annum. The note, which was prepared and signed by Virginia W. Simpson as Secretary/Treasurer of Santa Fe, was executed at the direction of Walter Wencke who was President and Chairman of the Board of Santa Fe.

18. On May 25, 1972, Santa Fe issued Check No. 2804 to Ramapo in the amount of $11,000. This check, which was signed by Virginia W. Simpson and Margery J. Hubbard on behalf of Santa Fe at Walter Wencke's direction, was endorsed and deposited into the account of Ramapo.

20. In exchange for Check No. 2804 in the amount of $11,000, Santa Fe received a promissory note in the sum of $11,000 with interest at the rate of eight percent (8%) per annum. This note was dated May 25, 1972 and executed by Potter, a Wencke lieutenant, as President of Ramapo.

21. On May 25, 1972, Ramapo issued Check No. 1 to PSI in the amount of $10,000 which was signed by Walter Wencke on behalf of Ramapo. The $1,000 remainder of the $11,000 lent to Ramapo by Santa Fe was utilized by Walter Wencke to pay the expenses of Ramapo, his private corporation. Subsequently, Check No. 1 was endorsed and deposited into the account of PSI.

22. In exchange for Check No. 1 in the amount of $10,000, Ramapo received a receipt from PSI dated May 25, 1972 signed by deLusignan on behalf of PSI.

23. By virtue of the above-stated transaction, the Court finds that Walter Wencke, through Ramapo, used said funds to obtain a majority interest in PSI (401,351 shares representing 53.5% of the outstanding common stock) for the sole benefit of his private corporation and family trust and to the detriment of Time and Santa Fe.

24. In violation of California Corporations Code Section 310, Walter Wencke failed to disclose to the minority shareholders of Time and Santa Fe the corporate opportunity encompassed in the Ramapo transaction. He further denied them their opportunity to approve or disapprove the so-called $11,000 "loan". Moreover, he failed to seek ratification of the diversion of the monies to Ramapo from Santa Fe, which in turn had obtained the money from Meti, Time's subsidiary.

25. During the period 1974 through 1976, Walter Wencke breached his fiduciary duty to time by causing Time, through Meti, to advance additional funds, for the benefit of PSI, amounting to $78,000. These funds were advanced on an unsecured basis, with no authorization by the relevant corporation and with no regard to the credit worthiness of the initial "borrower". Furthermore, there were no substantiating loan files, no credit reports or other documents normally undertaken in the regular course of business by a lending company.

26. Walter Wencke further breached his fiduciary duties by using Time, a public company, as his personal bank account to fund his private venture of preserving Ramapo's majority interest in PSI for the sole benefit of Ramapo, Hansa Trust, Potter, deLusignan and himself, and to the detriment of Time.

27. Walter Wencke, in conjunction with Potter and deLusignan, caused Kentfield Financial, Inc., a Delaware corporation, to be formed on September 22, 1972. At various times, these individuals served as officers and directors thereof. Kentfield was capitalized in February, 1973 by Ramapo to which Kentfield's common stock was originally issued without consideration.

28. Kentfield was utilized by Wencke as an additional conduit through which he could shield the diversion of these additional monies. The scheme employed by Wencke was as follows: Wencke directed the transfer of money from Time's subsidiary, Meti, through Kentfield, through Ramapo and finally, to PSI.

29. In violation of Section 13(a) [15 U.S.C. 78m(a)] and Section 14(c) [15 U.S.C. §78n(c)] of the Securities Exchange Act of 1934, Walter Wencke caused Time and Santa Fe to file with the Commission and transmit to their shareholders Information Statements relating to the respective companies' annual meetings purportedly held on December 15, 1972 and march 10, 1973, as well as file with the Commission Form 10-K Annual Reports for their fiscal years ending December 31, 1972 and May 31, 1972, respectively, all of which were materially false and misleading in that they failed to disclose the true and complete facts concerning the advance of money from Time's subsidiary, Meti, to Santa Fe to Ramapo. These documents further misrepresented that Walter Wencke received no compensation for the $11,000 "loan" when, as proved by the evidence, the money was used to fund his private venture from which he would profit.

30. In further violation of the above-cited federal securities laws, Walter Wencke caused Time to file with the Commission and transmit to its shareholders Form 10-K's for its fiscal years ending December 31, 1973 and 1974 and Information Statements for the annual meetings purportedly held on December 1, 1973 and November 2, 1974 which were false and misleading in that they failed to disclose the true and complete facts concerning the "loans" from Time's subsidiary, Meti, to Kentfield to Ramapo

and further failed to disclose that the funds were being advanced for the benefit of his private corporation, Ramapo, and family trust, The Hansa Trust.

31. In violation of California Corporations Code Section 310, Walter Wencke did not seek or obtain independent approval from Time, Meti and/or Santa Fe's boards of directors or the shareholders of these corporations to undertake the transactions described above.

32. The Court finds that during the period 1972 through 1976, Wencke owed fiduciary duties of good faith and fair dealing to said corporations and the minority shareholders thereof which were breached as follows:

(a) Wencke fraudulently caused said corporations to advance funds for Ramapo's account without disclosing the purpose and nature of said advances which was to secure and preserve for Ramapo, of which Wencke or his nominee owned 60%, a majority interest in PSI.

(b) Wencke caused the fruits of said advances to inure to his personal benefit. This self-dealing was at the expense and to the detriment of said corporations.

(c) Wencke, by taking the fruits of the advance of sums from Time, Meti and Santa Fe, usurped a valuable corporate investment opportunity of the said companies.

33. The acts and conduct of Wencke were oppressive, fraudulent, willful and malicious in that he knew that these actions were to the detriment of Time, Meti and Santa Fe and said actions were undertaken by him for his personal benefit at the expense of Time, Meti and Santa Fe.

34. Walter Wencke, and others in concert with him, in order to accomplish his fraudulent scheme to divert, hide and conceal

assets from creditors, including Time, Meti and Santa Fe, created the corporate and trust entities identified herein, as conduits and depositories for fraudulently obtained assets and for the purpose of sheltering, concealing and hiding the true ownership, possession and control of assets, and to hinder, delay and defraud creditors and minority shareholders.

35. Every conclusion of law contained in the foregoing Findings of Fact shall be deemed to be a conclusion of law as if set forth below as a conclusion of law.

CONCLUSIONS OF LAW

1. Pursuant to Section 22(a) of the Securities Act [15 U.S.C. § 77v(a)], Section 27 of the Exchange Act [15 U.S.C. § 78 aa], the Final Judgment entered herein and the inherent power of a court of equity to fashion effective relief, this Court has jurisdiction over the subject matter of the Receiver's Application.

2. Pursuant to the Final Judgment and Order Imposing Trust, this Court has personal and exclusive jurisdiction over The Ramapo Corporation and its assets and profits including, but not limited to, the 401,351 shares of Portsmouth Square, Inc. held of record by Ramapo and the dividend monies and profits derived therefrom.

3. Pursuant to the Final Judgment and Order Authorizing Disgorgement, this Court has exclusive jurisdiction over any "ill-gotten gains" wherever located, obtained from Time-Lenders, Inc., Santa Fe Financial Corporation and their past or present subsidiaries.

4. This Application is a post-judgment proceeding based in equity effectuated to carry out the mandate of the Final Judgment which requires the disgorgement of assets, profits and monies wrongfully taken from Time and Santa Fe.

5. The Ramapo Corporation, Kentfield Financial, Inc., The Hansa Trust and Theodore A. deLusignan have had actual notice and knowledge of the Final Judgment entered herein and this Application since on or about their filing with this Court. deLusignan has at various relevant times herein served as an officer, director, agent and/or employee of the corporate entities involved herein. In said capacities as well as in his individual capacity, he has actually participated in, conspired, and aided and abetted, either by affirmative action or by acceptance and/or enjoyment of the monies advanced and/or the fruits thereof, in the illegal acts and conduct set forth in the Findings of Fact.

6. At all relevant times, Walter Wencke was a controlling person of Time, its subsidiary, Meti, and Santa Fe within the meaning of Section 20 of the Securities Act of 1934 [15 U.S.C. § 78(b)]. Walter Wencke also controlled Ramapo and its subsidiary, Kentfield.

7. As delineated in the Findings of Fact herein, Time and Santa Fe's 10-K's for their fiscal years ended December 31, 1972 and May 31, 1972, respectively, contained untrue statements of material facts, omitted to state material facts necessary to make the statements made, in light of the circumstances under which they were made, not misleading, and failed to contain the information required by Rule 13a-1 and Form 10-K.

8. By reason of the foregoing acts, practices and courses of conduct, Wencke violated Section 13(a) of the Exchange Act [15 U.S.C. 78m(a)] and Rules 12b-20 and 13a-1 thereunder [17 C.F.R. 240.12b-20 and 240.13a-1].

9. As delineated in the Findings of Fact herein, Time and Santa Fe's Information Statements for their annual meetings purportedly held on December 15, 1972 and March 10, 1973, respectively, contained statements which, at the time and in light of the circumstances under which they were made, were false and misleading with respect to material facts and which omitted to

state material facts necessary in order to make the statements made not false or misleading, and failed to contain the information required by Rule 14c-2.

10. By reason of the foregoing acts, practices and courses of conduct, Wencke violated Section 14(c) of the Exchange Act [15 U.S.C. § 78n(c)], and Rules 14c-2 and 14c-6 thereunder [17 C.F.R. 240.14c-2 and 240.14c-6].

11. As delineated in the Findings of Fact herein, Time's Form 10-K's for its fiscal years ended December 31, 1973 and 1974 and Information Statements for its annual meetings purportedly held on December 1, 1973 and November 2, 1974 contained untrue statements of material facts, omitted to state material facts necessary to make the statements made, in light of the circumstances under which they were made, not misleading, and failed to contain the information required by Rule 13a-1, 14c-2 and Form 10-K.

12. By reason of the foregoing acts, practices and courses of conduct, Wencke violated Section 13(a) of the Exchange Act [15 U.S.C. § 78m(a)], Section 14(c) of the Exchange Act [15 U.S.C. § 78n(c)] and Rules 12b-20, 13a-1, 14c-2 and 14c-6 thereunder [17 C.F.R. 240.12b-20, 240.13a-1, 240.14c-2 and 240.14c-6].

13. Wencke acted in violation of California Corporations Code Section 310 in that he was an officer and director with a material financial interest in Time, Meti and Santa Fe and failed to present any facts as to the transactions with Ramapo or its subsidiary, Kentfield, to the disinterested directors and/or shareholders of Time, Meti or Santa Fe. Furthermore, once the transactions were consummated, Wencke failed to present said transactions to the disinterested directors of Time, Meti or Santa Fe for ratification or to the noninterested shareholders for approval.

14. Walter Wencke, as a director, officer and controlling person of Time, Meti and Santa Fe, violated federal securities laws

and regulations, violated state law and breached fiduciary duties he owed to said corporations as delineated herein in the Findings of Fact.

15. As a result of the above-described illegal activities of Walter Wencke and those acting in concert with him, the 401,351 shares of Portsmouth Square, Inc. held of record by Ramapo and the monies, profits and dividends derived therefrom are ill-gotten gains subject to the exclusive jurisdiction and disposition of this Court. Therefore, the Court concludes that Ramapo is an involuntary and constructive trustee holding said ill-gotten gains in constructive trust for the benefit of the shareholders of Time and Santa Fe.

16. The Receiver is entitled to disgorgement of any and all assets taken and misappropriated by Walter Wencke in violation of state or federal law or in breach of fiduciary duties as set forth in the Findings of Fact herein. Therefore, the Court finds that the ill-gotten gains described hereinabove at Paragraph 15 shall be disgorged to the Receiver in trust for the benefit of Time and Santa Fe.

17. The relief set forth in the Order is appropriate and necessary to carry out the mandates of the Final Judgment in this action by returning to innocent public shareholders assets which were looted from them.

18. Every finding of fact contained in the foregoing Conclusions of Law shall be deemed a finding of fact as if set forth as a finding of fact.

RECOMMENDATIONS

IT IS RECOMMENDED that the Findings of Fact and Conclusions of Law, as set forth hereinabove, be adopted by this Court.

IT IS FURTHER RECOMMENDED that this Court enter its Order

1) declaring that the 401,351 shares of Portsmouth Square, Inc. be disgorged to the Receiver, R. N. Gould, in trust for the benefit of the innocent public shareholders of Time-Lenders, Inc. and Santa Fe Financial, and

2) declaring that the assets and profits of The Ramapo Corporation derived from the 401,351 shares of Portsmouth Square, Inc. be disgorged to the Receiver, R. N. Gould, in trust for the benefit of the innocent public shareholders of Time-Lenders, Inc. and Santa Fe Financial Corporation.

IT IS FURTHER RECOMMENDED that the Receiver continue in his disgorgement proceedings consistent with the Findings of Fact and Conclusions of Law set forth herein.

DATED Oct. 7, 1983

HARRY R. McCUE, Special Master
United States Magistrate

No. 85-1896

Supreme Court, U.S.
FILED
JUN 17 1986
JOSEPH F. SPANIOL, JR.
CLERK

IN THE

Supreme Court of the United States

OCTOBER TERM, 1985

SECURITIES AND EXCHANGE COMMISSION,
Plaintiff,

v.

WALTER WENCKE, et al.,
Defendants.

THEODORE deLUSIGNAN,
Petitioner,

v.

R. N. GOULD, Receiver-Trustee,
Respondent.

RESPONDENT'S BRIEF IN OPPOSITION TO PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

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No. 85-1896

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STATEMENT OF THE CASE

The material facts and circumstances giving rise to the petition are fully set forth in the Opinion of the Ninth Circuit Court of Appeals which is included as Appendix A to the petition and which is herein incorporated by reference.

INTRODUCTION

The petition for writ of certiorari does not present to this Court any unique issues of statutory construction or constitutional import. This case was properly affirmed by the Ninth Circuit in a manner consistent with prior Supreme Court decisions and is predicated on a securities law disgorgement proceeding that does not present an appropriate vehicle for this Court's intercession. Combining these facts with the Ninth Circuit's findings that the petitioner failed to proceed diligently in the district court leads to the conclusion that this case is not suitable for this Court's review.

REASONS WHY THE PETITION SHOULD BE DENIED

I

THE NINTH CIRCUIT'S EXERCISE OF JURISDICTION WAS CONSISTENT WITH DECISIONS OF THIS COURT AND OTHER CIRCUITS

The district court's disgorgement order was directed exclusively at the assets of The Ramapo Corporation ("Ramapo"). It was not a judgment against the petitioner, Theodore deLusignan ("deLusignan"), nor did it seek any relief from him. Employing conventional judicial standards, both the district court and Ninth Circuit concluded that they possessed the requisite jurisdiction over Ramapo as well as the disgorged assets. In fact, the Ninth Circuit specifically found that the district court had personal

jurisdiction over both Ramapo and deLusignan. [Petition, p. A-7, fn. 5.][1]

The present petition does not originate from the entity (Ramapo) whose assets were disgorged nor is it derived from a shareholder's suit brought to protect a corporate right. Instead, it is brought by an individual (deLusignan), who seeks to unravel a legal proceeding involving assets of a corporation of which he is a minority shareholder. Ramapo did not appeal the disgorgement order nor is it a party to the petition.

deLusignan argues that the disgorgement order was improperly entered against him as a nonparty in a manner exceeding the district court's jurisdiction. This position is untenable for several reasons. First and foremost, the disgorgement order was directed exclusively at the assets of Ramapo, not deLusignan. Ramapo and its assets have been subject to the exclusive jurisdiction of the district court since 1977. [Petition, p. B-12, Conclusion of Law 2.] Second, the Ninth Circuit affirmed that Ramapo and deLusignan had been afforded notice and an opportunity to be heard and that there was no deprivation of their due process rights. [Petition, p. A-17.] Third, the Ninth Circuit held that as a result of the procedural safeguards employed during the disgorgement proceedings Ramapo and deLusignan had, essentially, been treated as intervening parties [Petition, p. A-10], and that the district court had personal jurisdiction over both [Petition, p. A-7, fn.5]. Finally, the credibility of deLusignan's argument is diminished by his failure to avail himself of the opportunities presented to him at the district court level.[2] As stated by the Ninth Circuit, "Nothing prevented

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[1] The February 19, 1986 Opinion of the United States Court of Appeals is reported at 783 F.2d 829 and is reprinted in the Petition's Appendix at pages A-1 through A-18. References to the Ninth Circuit Opinion will be made to the page number of said Appendix.

[2] The disgorgement process initiated with the entry of a Final Judgment on March 7, 1977, in *SEC v. Wencke*, Civil No. 76-0783-GT, United States District Court for the Southern District of California. It was followed by an Order

(Footnote continued on page 4)

deLusignan . . . from filing a responsive pleading to the disgorgement application or seeking discovery at any time between 1981 and the issuance of the district court's disgorgement order in November 1983." [Petition, p. A-15.] The Ninth Circuit also referred to deLusignan's failure to introduce evidence or question witnesses at the disgorgement hearing, his failure to make objections on the merits or request a continuance. [Petition, pp. A-15-17.] deLusignan's failure to participate at the district court level weighs against the suitability of this Court's review of this action.

Consistent with his lack of diligence at the district court level, deLusignan failed to note in the petition's Statement of Facts that on April 7, 1986, the mandate of the Ninth Circuit opinion was issued by the district court. At that time, deLusignan neither petitioned the Ninth Circuit for rehearing nor did he move, pursuant to Federal Rule of Appellate Procedure 41(b), for a stay of the mandate pending application to this Court for a writ of certiorari.

In support of his jurisdiction argument, deLusignan relies primarily on the Supreme Court cases of *Hansberry v. Lee*, 311 U.S. 32 (1940) and *Zenith Radio Corp. v. Hazeltine*, 395 U.S. 100 (1969), which were also considered by the Ninth Circuit. He fails to demonstrate to this Court any actual conflict between these cases and the Ninth Circuit Opinion. Rather than presenting an objective analysis of any purported conflict, deLusignan merely

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(Footnote continued from page 3)

Authorizing Disgorgement on March 27, 1979. Disgorgement Application No. 4 was then filed and served on deLusignan on April 22, 1981. Discovery was undertaken, including deLusignan's deposition on April 22, June 29-30, 1981. A noticed evidentiary disgorgement hearing was held before a United States Magistrate and Special Master on September 7, 1983, who then lodged his Findings of Fact, Conclusions of Law and Recommendations re Application No. 4 with the district court. [B-3 through B-16 of the Petition's Appendix.] A noticed hearing was then held before the district court on October 24, 1983, which entered its separate Order Adopting Findings of Fact, Conclusions of Law and Recommendations re Receiver's Application No. 4 in Disgorgement on November 7, 1983. [B-1 through B-2 of Petition.]

revives the arguments presented to the lower courts. deLusignan cites the *Hansberry* case for its holding that a party

> "is not bound by a judgment *in personam* in a litigation in which he is not designated as a party or to which he has not been made a party by service of process."

Hansberry v. Lee, supra, 311 U.S. at 40.

However, in the instant action, there exists no judgment *in personam* against deLusignan. The *Hansberry* holding is not applicable to deLusignan's situation. Additionally, he was *named* and *served* as a party to disgorgement. The principles of the *Hansberry* case do not conflict with the disgorgement proceedings.

The *Zenith* case is distinguishable in that it discusses the propriety of a judgment *in personam* directly against a corporation, Hazeltine Corporation, which was not a party to the action. deLusignan's attempt to align himself with the Hazeltine Corporation position is illogical since the disgorgement order is not a judgment *in personam* against him, but is directed at the assets of a corporation of which he is only a minority shareholder. For these reasons, the cited cases do not present this Court with a conflict and are consistent with the district court order and Ninth Circuit Opinion.

II

THE DISGORGEMENT PROCEDURES CONFORMED WITH THE FEDERAL RULES OF CIVIL PROCEDURE AND AFFORDED DELUSIGNAN DUE PROCESS

deLusignan's second argument is premised on his belief that the summary nature of the disgorgement proceedings did not comply with the Federal Rules of Civil Procedure. His argument is one of

form, not of substance, and it ignores the procedural safeguards which both the district court and the Ninth Circuit found to be sufficient to protect his due process rights.

The disgorgement proceeding employed by the district court was part of the receivership action, *Securities and Exchange Commission v. Walter Wencke, et al.*, Civil No. 76-0783-GT, United States District Court for the Southern District of California ("*SEC v. Wencke*"). The *SEC v. Wencke* case began with the filing of a complaint by the SEC in 1976 and has been litigated in a manner consistent with the Federal Rules of Civil Procedure. The disgorgement proceeding was not a new action and its subject matter was limited to the ill-gotten gains within the exclusive jurisdiction of the receivership court. Prior to this disgorgement application, the district court had held notice hearings wherein the disgorgement process was discussed and formulated in open court. Subsequently, an order was entered by the Court setting forth the purpose, goals and procedures of disgorgement and made a matter of public record.[3]

As the Ninth Circuit noted, although deLusignan was served with the disgorgement application more than two years prior to the disgorgement hearings, he failed to file a responsive pleading or seek discovery. [Petition, p. A-16.] At the disgorgement hearing, deLusignan was given the opportunity to introduce evidence and to call and cross-examine witnesses. Yet his counsel merely entered a "special appearance" and waived his opportunity to litigate the case on its merits. Finally, deLusignan failed to make any objections to the Findings of Fact and Conclusions of Law filed by the United States Magistrate and Special Master and did not request a continuance to do so. deLusignan was given the opportunity to take discovery and to file whatever responsive pleadings or briefs that he saw fit to do. The disgorgement court applied the Federal Rules of Evidence. A noticed Application was served upon deLusignan naming him, Ramapo and others as parties to

[3] Order Authorizing Disgorgement, March 27, 1979, *SEC v. Wencke, supra*. The Ninth Circuit referred to this Order at page A-4 of the petition.

disgorgement. deLusignan cannot now seriously claim that he lacked notice of the nature of the proceedings as well as an opportunity to be heard. In essence, deLusignan has attempted to argue that the disgorgement proceedings differed from the plenary process. What he fails to do is set forth any basis demonstrating that this purported difference substantially affected his rights or prejudiced him in any way. deLusignan received substantially all of the procedural protections that he would have been afforded if the disgorgement proceeding had been an independent, plenary action. Furthermore, the district court had the power to enter its *in personam* judgment against Ramapo, regardless of deLusignan's status in the disgorgement proceeding.

deLusignan cites *New Hampshire Fire Ins. Co. v. Scanlon*, 362 U.S. 404 (1960), in support of his contention that the disgorgement process was improper. He ignores the Ninth Circuit's well-reasoned analysis which specifically refers to the exceptions set forth in the *Scanlon* case [Petition, p. A-14, fn. 9) wherein summary proceedings were deemed acceptable:

> It is true that courts have sometimes passed on ownership of property in their custody without a plenary proceeding where, for illustration, such a proceeding was ancillary to a pending action or where property was held in the custody of court officers, subject to court orders and court discipline.

New Hampshire Fire Ins. Co. v. Scanlon, supra, 362 U.S. at 409-10. The disgorgement proceeding was not only ancillary to the pending *SEC v. Wencke* action, but also involved assets held by the federal court-appointed receiver. The Ninth Circuit recognized the applicability of these exceptions and cited cases from four other circuits where summary proceedings were employed. [Petition, p. A-14, fn. 9.] Moreover, deLusignan incorrectly asserts at page 16 of his petition that the Ninth Circuit determined that, "there was no *in rem* jurisdiction over petitioner's Ramapo shares or Ramapo's PSI shares." Review of the Opinion reveals that the

Ninth Circuit did not find it necessary to resolve that issue since it concluded that, "We need not decide the precise extent of the district court's *in rem* jurisdiction, however, in light of our conclusion that the district court had personal jurisdiction over both Ramapo and deLusignan." [Petition, p. A-7, fn. 5.]

deLusignan implies that the Ninth Circuit approval of the use of summary proceedings in the disgorgement proceeding will have widespread consequences necessitating this Court's exercise of its supervisory power. To the contrary, the Ninth Circuit Opinion is limited to post-judgment proceedings in the unique circumstances of a securities receivership wherein it is ancillary to an existing action, where adequate procedural safeguards are employed and the court has jurisdiction over the necessary parties.

The Ninth Circuit's reliance on *SEC v. Universal Financial*, 760 F.2d 1034 (9th Cir. 1985) is well-founded. The *Universal Financial* case is similar in that it also involved a large-scale securities receivership with a complex myriad of transactions, investors and creditors. The summary proceedings utilized in *Universal Financial* employed procedural safeguards very similar to the case at bar.

deLusignan claims that the present case is distinguishable from *Universal Financial* for, among other reasons, the fact he had no time for discovery, briefing and trial preparation and that there was no mechanism by which to answer or bring a motion. The Ninth Circuit found differently. As the Ninth Circuit stated, from the beginning of this disgorgement application until the entry of the disgorgement order in November 1983, "DeLusignan did nothing during that time on behalf of himself or Ramapo." [Petition, p. A-16.] If there was one common thread that permeates both cases, it was that the procedural safeguards afforded the interested parties were more than sufficient to ensure their respective right to due process of law.

The Federal Rules of Civil Procedure are guidelines designed to "be construed to secure the just, speedy, and inexpensive determination of every action." Rule 1 of the Federal Rules of Civil Procedure. As Mr. Justice Black has stated, "The principal function of procedural rules should be to serve as useful guides to help, not hinder, persons who have a legal right to bring their problems before the courts." Order Adopting Revised Rules of the Supreme Court, 346 U.S. 946 (1954). This is also true of the Fifth Amendment right to due process. "Due process is flexible and calls for such procedural protections as the particular situation demands." *Morrissey v. Brewer*, 408 U.S. 471, 481 (1972). Accordingly, this policy of flexibility eliminates the need for this Court to exercise its supervisory power over the Ninth Circuit's approval of the summary disgorgement proceedings.

CONCLUSION

The petition seeks to burden this Court with the review of a decision the effect of which is procedural and limited. Moreover, deLusignan's petition is actually a request for this Court to break new legal ground. Carried to its logical conclusion, deLusignan's argument would have this Court require a corporation's shareholders to be named and served as parties to any action which seeks *in personam* relief solely against that corporation.

The decision of the Ninth Circuit will facilitate the enforcement of the federal securities laws and is in the best interests of the general public. The decision below is correct and well-reasoned. It is consistent with this Court's prior interpretations of the Fifth Amendment right to due process and is not in conflict with prior decisions of this Court or other circuits.

The Receiver respectfully submits that the petition for a writ of certiorari should be denied.

Respectfully submitted,

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